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Mexico

COTTON AND PRODUCTS ANNUAL

Mexican Cotton Production to Decline

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Report Highlights:

MY 2009/10 cotton production is forecast at 450,000 bales, 20.6 percent lower than last year's revised estimated production. Rising energy costs and producers switching to more profitable crops will continue to hamper cotton production. However, the United States is expected to maintain its dominant market share of cotton imports as practically all cotton imports are sourced from the United States. MY 2009/10 cotton imports are forecast to increase slightly to 1.5 million bales in MY 2009/10 in order to cover domestic demand.

Executive Summary:

Similar to other countries, Mexico's economy has been significantly affected by the international financial crisis, which has reduced growth possibilities for 2009. Although the gross domestic product (GDP) increased 1.3 percent in 2008, several private analysts and the GOM have forecast that Mexico's GDP could decline three percent in 2009. Under this scenario, consumer purchasing power should be adversely affected and a decline in the growth of apparel spending is expected.

Therefore, MY 2009/10, cotton production is forecast at 450,000 bales, 20.6 percent lower from last year's revised estimated production. A decrease in cotton planted area for MY 2008/09 was seen due as significant increases in input costs, particularly fuel and fertilizers led to producers selecting alternative crops. MY 2007/08 cotton production planted and harvested areas were kept unchanged to reflect official data from the Secretariat of Agriculture, Livestock, Rural Development, Fisheries and Foodstuffs (SAGARPA) and final information from private sources.

Domestic demand for MY 2009/10 is forecast at 1.83 million 480 lbs. bales, which is a five percent decrease compared to the previous year. The decrease is due to a drop in demand for textile products as a result of the slowdown in consumer purchasing power. Consumer demand for textile products also declined in MY 2008/09 as a result of the slowdown in the U.S. economy.

The United States is expected to maintain its dominant market share of cotton imports in MY 2009/10, as practically all cotton imports are sourced from the United States and lower production should increase imports to 1.45 million bales. At the same time, demand for apparel and textile products will likely decrease next year as Mexico's apparel and textile exports continue to lose market share in the United States. For MY 2008/09, the 1.4 million imported bales will supply nearly 70 percent of Mexico's needs in the textile industry. The cotton import estimate for MY 2007/08 has been kept unchanged according to official information from the Secretariat of Economy (SE). The export estimate for MY 2009/10 is forecast at 120,000 bales. The MY 2008/09 export estimate has been revised downward.

With production declining in MY 2009/10, ending stocks are projected to decline to 800,000 bales. Since imports have been declining in MY 2008/09, the ending stocks were revised downward to 845,000 bales.

Commodities:

Cotton

Production:

Total Mexican cotton production for marketing year MY 2009/10 (Aug-Jul) is forecast at 450,000 bales, down a dramatic 20.6 percent from last year's estimate. This is attributed to several factors that have affected not only the cotton sector but the entire Mexican agricultural sector. According to the Confederation of Mexican Cotton Associations (CMCA), a primary factors were the reduction in the government set target price for cotton, increased input costs (particularly fuel and fertilizers), and the decision of many growers to consider planting alternate commodities that could be more profitable during 2009.

The GOM target price for the 2009 growing season, which is then used to determine GOM support payments to producers, was set at \$42.02 (USD) cents per pound. In recent seasons, the target price has been set at \$67.75 (USD) cents per pound, which contributed to an average of 650,000 480 bales per cycle. However, the cotton sector is confident that they are in the position to overcome this negative situation since most of the main cotton producing areas in Mexico are best-equipped to grow only cotton. More importantly they believe they can overcome because their people are committed to this labor and the specialized machinery mixed in with their experience will push them through these tough times.

MY 2008/09 production figures were revised downward. The occurrence of harsh weather and diseases in some production areas, along with the lack of financing for planting, reduced production from previous expected levels. The MY 2007/08 production number remains unchanged, reflecting official data.

The cotton planted area, yield, and production (estimate and forecast) by state for MY 2008/09 and MY 2009/10 are as follows:

| Table 1. Mexico: Cotton Production by State/Region | | | | | | |
|---|----------------------------|-------------------------|---------------------------|---------------------------|-------------------------|---------------------------|
| Region | MY2008/09 estimated | | | MY2009/10 forecast | | |
| | Planted Area (Has) | Yield (Bales/Ha) | Production (Bales) | Planted Area (Has) | Yield (Bales/Ha) | Production (Bales) |
| South Sonora | 2,000 | 6.33 | 12,656 | 2,000 | 5.0 | 10,000 |
| North Sonora | 300 | 5.0 | 1,500 | 0 | 0 | 0 |
| Mexicali, BC | 22,905 | 6.26 | 143,420 | 15,300 | 6.0 | 91,800 |
| Juarez, Chih. | 37,007 | 4.23 | 156,716 | 17,500 | 5.0 | 87,500 |

| | | | | | | |
|----------------------|----------------|-------------|----------------|---------------|-------------|----------------|
| Delicias, Chih. | 1,558 | 6.45 | 10,048 | 500 | 5.0 | 2,500 |
| Ojinaga-Aldama Chih. | 19,770 | 5.84 | 115,565 | 12,000 | 5.8 | 69,600 |
| La Laguna Dgo-Coah. | 16,415 | 7.58 | 124,344 | 20,000 | 7.0 | 140,000 |
| North Tamaulipas | 1,100 | 2.4 | 2,633 | 0 | 0 | 0 |
| TOTAL | 100,955 | 5.62 | 566,882 | 67,300 | 5.96 | 401,400 |

Source: Confederation of Mexican Cotton Associations

Cotton yields around the main cotton producing areas vary significantly. Average cotton yields for MY 2009/10 are expected to reach 5.96 bales/ha with a range of between five and seven bales per hectare. The highest yield/ha is expected in the La Laguna region where cotton growers have adopted the use of genetically modified seed varieties. The CMCA stated that biotechnology continues to be an important tool in reducing pesticide use by more than 50 percent as well as stimulating an increase in yields. At this point, it is uncertain the acreage intended to be planted with genetically modified seeds varieties since the Mexican peso exchange rate against the U.S. dollar is not enticing the use of genetic seed. However, producers are aware of the benefits genetically modified seeds could provide for production purposes since they are obtaining yields around six bales per hectare while in the past conventional seeds produced yields of 3.5 bales per hectare. It is expected that this improved seed will be planted mainly in Chihuahua, Mexicali and the La Laguna region (Coahuila and Durango states), which all have the best infrastructure and resources to use this seed. Other factors that have influenced the gradual yield increase in the past few years include improving the cultural practices, such as: narrow furrows, better prevention methods against diseases, and the investment of new combines. Preliminary estimates from SAGARPA indicate that the production of Genetically Modified Cotton in 2008 was 12,629 MT.

The cost of production has increased since most of the inputs are valued in U.S. dollars. For example, the La Laguna region requires investment around \$2,222 (USD) per hectare.

Recently, SAGARPA published a notice that modifies the operational rules of PROCAMPO; the Mexican domestic agricultural support program for the 2009 to 2012 crop cycles. The new supports will be between 963 to 1,300 pesos per hectare (USD \$71.07- 95.94/ ha), depending on the number of hectares each producer has registered in the program.

Additionally, SAGARPA has reduced the maximum payment limit under the program to 100,000 pesos (roughly USD \$7,380.00) regardless of total area under production.

According to the CMCA, the quality of the MY 2008/09 crop is similar to averages from recent years, especially in growth. In general, the quality of Mexican cotton is poor. There are approximately 150 gin mills in Mexico: 23 in Chihuahua, 15 in the La Laguna region, 12 in San Luis Rio Colorado, and the rest in other states. The majority of the mills are

outdated and tend to damage cotton during the ginning process. In some areas (mainly in Chihuahua, Ojinaga, and the Mexicali cotton areas), Mexican growers have been investing in modern gin mills. Large textile firms continue to use Universal HVI Calibration Cotton Standards to sort the cotton by fiber length, strength, micronaire (a measure of the cotton's fineness), color grade, color Rd (reflectance), color +b (yellowness), and trash percentage. Due to only a few of the Mexican growers using such standards, domestic cotton is typically used by smaller mills.

Consumption:

Mexico's outlook is less favorable than the previous year as economic growth is expected to be negative in 2009 due to the turmoil in the world economy. MY 2009/10 consumption is projected at 1.83 million 480 lbs. bales as a result of sluggish demand from the Mexican textile industry, which reflects the impact of an economic slowdown and a relatively lower level of consumer purchasing power for apparel spending. The total consumption estimate for MY 2008/09 was kept unchanged based on updated information from industry sources.

Trade:

Cotton imports are forecast to increase slightly from 1.4 million bales in MY 2008/09 to 1.5 million bales in MY 2009/10 in order to cover the domestic demand in light of a significantly decreased production. However, exchange rate fluctuations will undoubtedly play a key role in determining the amount to be imported. Nonetheless, the United States should continue to be the main supplier to Mexico, accounting for practically 100 percent of total cotton imports. The import estimate for MY 2007/08 was kept unchanged reflecting official data from the Secretariat of Economy (SE).

Mexican cotton exports are expected to decrease to 120,000 bales in MY 2009/10, according to private industry sources. The Mexican cotton industry is still vulnerable to the effects of a U.S. economic slowdown reducing Mexico's textile exports to the United States, alongside the fact that Asian countries (mainly China) continue displacing Mexican exports to the United States. The export figures for MY 2008/09 have been adjusted downward due to a decreased production and the above mentioned slowdown in the U.S. economy.

The MY 2007/08 export figures were kept unchanged reflecting revised information from the SE and the industry, respectively.

Trade Matrices

| Table 2. Mexico: Cotton Exports | | | |
|---------------------------------|-------------------------------------|--------------|---------------|
| Cotton | H.T.S. 52010002, 52010003, 52010099 | | Units: MT |
| Exports to: | MY 2006/2007 | MY 2007/2008 | MY 2008/2009① |
| U.S. | 446 | 64 | 0 |
| China | 16,770 | 36,979 | 8,019 |
| Japan | 1,127 | 1,361 | 1,219 |
| Vietnam | 4,872 | 670 | 7,669 |
| Others not listed | 18,788 | 12,330 | 16,907 |

| | | | |
|-------------|--------|--------|--------|
| Grand total | 42,003 | 51,404 | 20,408 |
|-------------|--------|--------|--------|

SOURCE: World Trade Atlas, MY begin August ends July. • Data as of January 2009

| Table 3. Mexico: Cotton Imports | | | |
|---------------------------------|-------------------------------------|--------------|---------------------------|
| Cotton | H.T.S. 52010002, 52010003, 52010099 | | Units: MT |
| Imports from: | MY 2006/2007 | MY 2007/2008 | MY 2008/2009 ^① |
| U.S. | 300,311 | 357,253 | 160,274 |
| Egypt | 418 | 509 | 146 |
| Others not listed | 0 | 491 | 29 |
| Grand total | 300,729 | 358,253 | 160,449 |

SOURCE: World Trade Atlas, MY begin August ends July. • Data as of January 2009

| Table 4. Mexico: Cotton Yarn Exports | | | |
|--------------------------------------|-------------------------|---------|-----------|
| Cotton Yarn | H.T.S. 5205, 5206, 5207 | | UNITS: MT |
| Exports to: | CY 2006 | CY 2007 | CY 2008 |
| United States | 11,897 | 8,232 | 8,079 |
| Canada | 447 | 306 | 411 |
| Guatemala | 686 | 628 | 744 |
| Colombia | 2,810 | 9,066 | 5,684 |
| Other not listed | 1,464 | 2,589 | 3,873 |
| Grand Total | 17,304 | 20,821 | 18,791 |

SOURCE: World Trade Atlas.

| Table 5. Mexico: Cotton Yarn Imports | | | |
|--------------------------------------|-------------------------|---------|-----------|
| Cotton Yarn | H.T.S. 5205, 5206, 5207 | | UNITS: MT |
| Imports from: | CY 2006 | CY 2007 | CY 2008 |
| United States | 36,910 | 20,391 | 20,966 |
| El Salvador | 943 | 892 | 857 |
| Spain | 1,483 | 1,042 | 1,501 |
| South Korea | 1,919 | 1,792 | 1,959 |
| Other not listed | 2,301 | 1,358 | 1,691 |
| Grand Total | 43,556 | 25,472 | 26,974 |

SOURCE: World Trade Atlas.

| Table 6. Mexico: Woven Cotton Fabric Exports | | | |
|--|-------------------------------------|------------|-----------------------|
| Woven Cotton Fabrics | H.T.S. 5208, 5209, 5210, 5211, 5212 | | UNITS: M ² |
| Exports to: | CY 2006 | CY 2007 | CY 2008 |
| United States | 17,584,541 | 17,449,843 | 15,873,695 |
| Colombia | 14,092,355 | 22,230,820 | 17,335,240 |
| Guatemala | 456 | 997 | 4,718,753 |
| Kenya | 0 | 0 | 2,568,475 |
| Other not listed | 7,535,108 | 28,973,477 | 12,093,844 |
| Grand Total | 39,212,460 | 68,655,137 | 52,590,007 |

SOURCE: World Trade Atlas.

| Table 7. Mexico: Woven Cotton Fabric Imports | | | |
|--|-------------------------------------|-------------|-------------|
| Woven Cotton | UNITS: M ² | | |
| Fabrics | H.T.S. 5208, 5209, 5210, 5211, 5212 | | |
| Imports from: | CY 2006 | CY 2007 | CY 2008 |
| United States | 388,538,880 | 372,749,889 | 213,195,062 |
| China | 160,838,389 | 68,076,153 | 152,912,427 |
| Brazil | 13,795,418 | 18,032,838 | 42,616,092 |
| Spain | 19,341,288 | 12,492,889 | 12,800,182 |
| Guatemala | 16,034,892 | 13,503,845 | 22,971,318 |
| PAKISTAN | 18,074,422 | 22,454,068 | 26,555,882 |
| Other not listed | 221,867,542 | 127,810,151 | 68,712,874 |
| Grand Total | 683,227,833 | 553,601,140 | 539,763,837 |

SOURCE: World Trade Atlas.

Stocks:

MY 2009/10 ending stocks are forecast to decline around five percent to 800,000 bales, with the overall decrease in domestic stocks slightly offset by the increase in cotton imports. Due to a lower than previously estimated cotton production for MY 2008/09, the ending stock number has also been decreased in comparison to previous forecasts.

Marketing:

According to the National Cotton Council, although Mexico is losing shares in the U.S. market to low cost producing Asian countries, Mexico was once again one of the largest exporters of cotton goods to the United States in 2008.

Industry consultants have reported that in order to remain the major supplier of textiles and apparel to the United States, Mexican firms should continue their efforts of shifting production from low-value-added basic garments to high-quality and technology intensive products. However, a stagnant textile sector may hamper the accomplishment of these projects in the short-medium term.

In December 2008, sales to specialized apparel stores declined 15 percent, the import of shirts and blouses decreased 69 percent, and imports of cotton sweaters and vests decreased 51 percent.

Production, Supply and Demand Data Statistics:

Table 8. Mexico: Cotton PSD Table

| PSD Table | | | | | | | | |
|-------------------|----------------------------------|--------------------------|----------------------------------|--------------------------|----------------------------------|--------------------------|----------------|-----|
| Country | Mexico | | | | | | | |
| Commodity | Cotton | | | | | | | |
| | (HECTARES) | | 1000 480 lb. Bales | | (PERCENT) | | (KG/HA) | |
| | 2007/08 | | 2008/09 | | 2009/10 | | | |
| | Annual Data Displayed | New Post Data | Annual Data Displayed | New Post Data | Annual Data Displayed | New Post Data | | |
| Market Year Begin | 08/2007 | | 08/2008 | | 08/2009 | | | |
| Area Planted | 113 | 113 | 120 | 120 | 110 | 0 | 0 | 100 |
| Area Harvested | 110 | 110 | 101 | 115 | 101 | 0 | 0 | 70 |

| | | | | | | | | | |
|---------------------------|-------|-------|-------|-------|-------|-------|---|---|-------|
| Beginning Stocks | 1,027 | 1,037 | 1,037 | 932 | 933 | 933 | 0 | 0 | 845 |
| Production | 620 | 621 | 621 | 615 | 680 | 567 | 0 | 0 | 450 |
| Imports | 1,530 | 1,500 | 1,500 | 1,300 | 1,400 | 1,400 | 0 | 0 | 1,450 |
| MY Imports from U.S. | 0 | 0 | 1,500 | 0 | 0 | 1,400 | 0 | 0 | 1,450 |
| Total Supply | 3,177 | 3,158 | 3,158 | 2,847 | 3,013 | 2,900 | 0 | 0 | 2,745 |
| Exports | 220 | 200 | 200 | 150 | 200 | 130 | 0 | 0 | 120 |
| Use | 2,000 | 2,000 | 2,000 | 1,800 | 1,900 | 1,900 | 0 | 0 | 1,800 |
| Loss | 25 | 25 | 25 | 25 | 25 | 25 | 0 | 0 | 25 |
| Total Dom. Cons. | 2,025 | 2,025 | 2,025 | 1,825 | 1,925 | 1,925 | 0 | 0 | 1,825 |
| Ending Stocks | 932 | 933 | 933 | 872 | 888 | 845 | 0 | 0 | 800 |
| Total Distribution | 3,177 | 3,158 | 3,158 | 2,847 | 3,013 | 2,900 | 0 | 0 | 2,795 |
| Stock to Use % | 42 | 42 | 42 | 45 | 42 | 42 | 0 | 0 | 42 |
| Yield (KG/HA) | 1,227 | 1,229 | 1,229 | 1,326 | 1,287 | 1,222 | 0 | 0 | 1,400 |

Author Defined: Textile Industry

Similarly, the textile industry has been under pressure from foreign suppliers and various economic factors; thus growth in consumption within this sector has been stagnant. Industry sources estimate that this trend will likely continue in MY 2009/10. According to the Mexican Textile Industry (CANAITEX), the textile industry was one of the most affected sectors by the end of 2008. The economic recession in Mexico, increased rates for energy, and a decrease in sales have compelled a decrease in production. Thus, the closure of companies was an increasing trend during 2008 resulting in 29,000 layoffs. The main users of Mexican cotton are the textile industry and the oil industry. A preliminary industry figure indicates that sales in this sector were eight percent lower compared to the same period the previous year.

Despite the fact that Mexico's apparel and textile industry expanded as a result of NAFTA, it has been declining the past few years. The Mexican market share of cotton apparel peaked in 2000, and in the past seven years, Mexican shipments have been declining. This decline is almost exclusively attributed to the fact that Mexico's apparel and textile industry is losing domestic and U.S. market share to low cost producing countries such as China.

The textile output has been declining for four consecutive years. Many sources have stated that due to sluggish domestic consumption looking for cheaper foreign low-quality garments, despite the question of legal origin, this trend could continue for the next couple of years. According to the President of the Mexican Textile Industry Chamber (CANAITEX), the textile industry is at a critical stage due to a declining output the past three years.

The textile sector's main problems can be summarized as follows:

- A loss of market share in the United States;
- Foreign competition in the domestic market;
- Rising energy costs, mainly electricity costs;
- Increased taxes;
 - Tighter Credit Access;
 - Logistic and transportation costs to import cotton;
 - Domestic competition of illegal merchandises.

Industry sources report that Mexico has lost volume in the key categories of knit and woven shirts and bottoms in recent years. However, the above cited factors continue to hamper the competitiveness of the Mexican apparel industry. The outlook for 2009 does not support a dramatic shift in these key factors. Furthermore, the deceleration in U.S. economic growth would not contribute to offset this scenario, which could mean that the volume of Mexican imports may decline even further.

Regarding the domestic market, industry sources have stated that six of each 10 garments are supplied illegally (through contraband, stolen merchandise, and/or products manufactured without paying the proper taxes). Likewise, the formal clothing market is highly concentrated; only nine purchasing companies represent more than 40 percent of the total clothing sold.

Industry sources have commented that energy costs are extremely expensive, thus making it difficult for the domestic industry to cut costs.

Mexico is competitive in the production of fibers as well as the cutting, assembly and export of garments. However, Mexico has not been able to produce quality fabric that is required for apparel. Mexico still relies heavily on imported textiles. It's well known that Mexico's textile industry is focused on the production of fashion, artisanal fashion and prêt-à-porter (ready to wear) garments. Industry sources report that the creation of a commodity chain, which uses Mexican textiles as the main input and has the capacity to deliver a fully packaged product with more value-added services, is the key to the survival of the Mexican textile sector.